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C O N F I D E N T I A L SECTION 01 OF 03 BEIJING 022299

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SUBJECT: CENTRAL CHINA EXPO 2006: RHETORIC BUT FEW RESULTS

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Classified By: (C) CLASSIFIED BY DEPUTY MINISTER COUNSELOR FOR ECONOMIC
AFFAIRS CHRISTOPHER BEEDE; REASON 1.4(B) AND (D).

SUMMARY

¶1. (C) Central China Expo 2006, held in Changsha, Hunan Province in late September, officially launched the Central Government's Central China Rising initiative to balance geographical development by bolstering economic prospects in the region's six provinces. Although the Expo had high-level support, including the attendance of Vice Premier Wu Yi and Minister of Commerce Bo Xilai, the tangible results were confined primarily to limited opportunities for selling higher-quality consumer products and investing in the information technology sector. In response, most potential investors we talked to assessed few viable business opportunities in the region. A notable exception was the significant Hong Kong presence, with many of those participants encouraged by Central China's progress. Several American investors already operating in Changsha shared the Hong Kongers' outlook. These optimistic views notwithstanding, current trends suggest that for the short term, most investment in Central China will continue to be large government-sponsored fixed asset investment projects.
END SUMMARY.

TRAVEL TO HUNAN

¶2. (C) Econoff and Conoff visited Hunan Province September 24-29 and attended Central China Expo events in Changsha, the provincial capital, on September 25-27. Emboffs attended Expo events, including the Central China Business Summit, which Vice Premier Wu Yi opened, and met with the Deputy Governor of Hunan Province. Emboffs also interviewed business managers, government officials, and academics in Changsha and Beijing for this report.

BEIJING PROMOTING "CENTRAL CHINA RISING"

¶3. (C) Central China -- consisting of 360 million people in the six provinces of Henan, Hunan, Hubei, Anhui, Jiangxi, and Shanxi -- lags far behind many of China's coastal regions in terms of wealth and industrial development, in great part because of the economics of transporting goods to ports using

the limited infrastructure in place to date (a situation that is set to improve rapidly). Zhang Jun, a researcher specializing in Central China at the China Academy of Social Sciences in Beijing, commented that this legacy has left Central China oriented towards old-style central economic planning with a resulting dependence on state-owned enterprises (SOEs) in the industrial sector. Economic planners in Beijing have been sensitive to Central China's challenges over the years and began conceptually pondering the Central China Rising initiative as early as the mid-1990s, explained Zhang.

14. (C) Central China already has established itself as a transportation hub and a base for energy projects, but with a dense population and a large percentage of rural residents, the Central Government now recognizes that it cannot afford to ignore central China, Zhang told us. The six provincial governments remain committed to funding fixed asset investment (FAI) projects to improve infrastructure, he said.

One goal of the Central China Expo also was to complement their efforts by encouraging increased private sector participation in the economy. Zhang does not believe the Central Government views FAI in Central China as an economic overheating issue but rather as an instrumental part of promoting balanced regional development. Separately, Wang Zili, Director of the Institute of International Relations at the Hunan Academy of Social Sciences, said that the Central China Rising initiative finally elevates the region's status and demonstrates that the Central Government no longer intends to ignore Central China in favor of the industrial Northeast or the impoverished West (reftel).

15. (C) The Central China Rising initiative aims to encourage provincial governments to pool resources, labor, and capital.

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To this end, Shanxi Province has now been officially added as Central China's sixth province. At a press conference on September 27 in Changsha during the Expo, Minister of Commerce Bo Xilai and Shanxi Provincial Governor Yu Youjun emphasized that Shanxi will be the primary supplier of energy resources for Central China under the new six-province orientation, and they announced that Taiyuan, Shanxi's provincial capital, will host the first China International Coal and Energy New Industry Exposition (CICEN Expo) in September 2007.

HIGH-LEVEL SUPPORT AT CENTRAL CHINA EXPO 2006

16. (U) At the Central China Expo's opening event, the Central China Business Summit, Commerce Minister Bo stated that the participation of Vice Premier Wu Yi demonstrated the Central Government's commitment to Central China. The Vice Premier encouraged the six provinces to take advantage of the opportunity and utilize the region's comparative advantages, including energy resources, industrial capability, and its strong agricultural base. Xu Kuangdi, Vice Chairman of the CPPCC, stated that Central China's biggest challenge will be to manage the region's urbanization and rural-to-urban migration, particularly given the large rural population in provinces such as Henan and Hunan. Governors from all six provinces attended the Expo, and all of them delivered speeches at the Business Summit, each emphasizing respective resource bases and investment opportunities.

LOOKING TO HONG KONG

17. (C) Leading a large delegation to Changsha, Hong Kong Chief Executive Donald Tsang said his city can play a role in Central China in three ways: 1) Attracting investors and capital to the region, 2) Assisting enterprises based in Central China in upgrading their industries and promoting brand-name products, and 3) Enhancing the quality of the region's service industries. Tsang also cited several

examples of increasing economic cooperation and integration between Hong Kong and Central China.

¶8. (C) Zhou Yilei, Marketing Executive for the Hong Kong Trade Development Council (HKTDC), told Econoff that the official Hong Kong delegation at Central China Expo exceeded 150 people. Zhou, whose office was established in Wuhan in 1994, noted big changes in Central China and its relationship with Hong Kong in the intervening period. Hong Kong's primary interest in the region remains the service sector, Zhou said, but there are also manufacturing opportunities closer to home in Hunan and Jiangxi.

OPPORTUNITY KNOCKS FOR SMEs...MAYBE

¶9. (C) Representatives of small- and medium-sized enterprises (SMEs) told Econoff that development in coastal areas is increasingly saturated, making the interior more attractive. Leo Lam, General Manager of ELM Computer Technologies in Hong Kong, said that saturation in the information technology (IT) industry leaves him more likely to explore opportunities in Changsha or Wuhan than in Guangzhou or Shenzhen.

¶10. (C) Gary Zou, Chief Economist at Ameribankers Corporation, disagreed with Lam's assessment, saying that his U.S.-based clients are not yet interested in investing in Central China primarily because investment incentives in the region are not good enough to compete with time-tested opportunities on China's coast. Although Central China's Hunan Province offers a 33 percent income tax break, it is not enough to convince a typical foreign investor to move to the interior, which still is an unknown quantity.

SOME U.S. COMPANIES SEE OPPORTUNITY...

¶11. (C) Large U.S. companies that already have invested in Central China told Econoff that they are pleased with the results. Zheng Jian, Sales and Marketing Director for Hunan COFCO Coca-Cola (a share-holding company 35 percent owned by Coca-Cola) said that Coca-Cola sales in Hunan Province have grown 30 percent annually on average, and he expects sales to

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increase further with more urbanization, as 60-70 percent of sales are in urban areas. Coca-Cola expects to open a production factory in Jiangxi Province within the next two to three years, Zheng said, due to increasing sales in that province. Steven Jiang, Walmart's Regional Corporate Affairs Manager, said that Central China's market presents many opportunities for good quality consumer products. Walmart now has nine stores in Central China's six provinces, including three outlets in Hunan Province, and two each in Jiangxi and Hubei. The company plans to expand to at least 25 stores in the region the next three years, according to Jiang.

...BUT OTHER NOT IMPRESSED

¶12. (C) Lily Young, Events Executive at the American Chamber of Commerce in Beijing, agreed that companies selling consumer products provide the best opportunity for U.S. firms, but she said that representatives from the twenty-four U.S. companies (including Cargil and Oracle) who she accompanied to Changsha were disappointed with the Expo. Yuen Yee Jing, Advisor to California Industrial City in Zhengzhou, added that he believes the Expo was too government-driven and failed to attract potential investors who could be matched with investment opportunities in the region. James Liu, Manager of Government Affairs for Honeywell's office in Beijing, told Econoff in mid-September that Honeywell would not send anyone to the event. Without clear incentives for investing in the region, Liu said, Central China is just one more region that is "rising" with

the Northeast Revitalization and the Great Western Development Program both already underway. If all of China's regions are rising, Liu noted, then in reality, none of them are.

COMMENT, PART ONE: LICENSE FOR OVERHEATING IN CENTRAL CHINA

¶13. (C) Central Government officials have made clear their intention to continue with plans for infrastructure improvements in Central China, in contrast with other parts of China (such as Inner Mongolia) where the Central Government has voiced concerns about overheating. No one we talked with expressed concern about possible efforts to slow high rates of FAI in the six provinces. With a low industrial and infrastructure base and extensive public works improvements on the drawing board, continued high FAI growth in Central China appears to have been deemed acceptable in the context of national efforts to balance regional development.

COMMENT, PART TWO: SLEEPING IN CHANGSHA

¶14. (C) Changsha lacks the economic dynamism of Wuhan, or even Zhengzhou, and many participants wondered what kind of backroom political maneuvering led to its hosting the region's first major trade and investment event. Zhengzhou in 2007 and Hefei in 2008 may be better equipped to host the Central China Expo, but they will have to overcome Changsha's legacy of a poorly organized event that featured little participation by serious investors. There were, for example, so few visitors on the second day of the Expo that Emboffs found many booths either vacant or with booth attendants sleeping soundly. END COMMENT.

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